

May 28, 1953

To : Assistant Controllers
Examination Staff

From : Leslie Surginer, Controller
Division of the Controller

Subject: Interim Field Conferences
Cheyenne, Wyoming - December 8-12, 1952
Old Point Comfort, Virginia - January 12-16, 1953

Summary of Composite Minutes

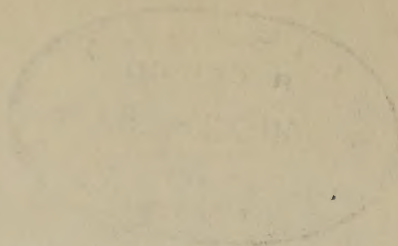
Transmitted herewith is a summary report of the presentations and discussions which occurred during the interim conferences of the Telephone Loans, Telephone Engineering, and Controller Divisions held at Cheyenne, Wyoming, December 8-12, 1952, and Old Point Comfort, Virginia, January 12-16, 1953.

The discussions at these conferences were of particular importance, principally because these were the first general field meetings devoted chiefly to the telephone program and because specific internal audit and internal control appraisal programs were presented and explained to the field staff.

We strongly recommend that you review this material. We believe you will find it useful in properly executing your daily assignments.

Attachment

Leslie Surginer



May 28, 1953

Assistant Controller
Washington State

From: Leslie Ferguson, Controller
Division of the Controller

Subject: Internal Field Conference
Chairman: James J. Anderson, May 1953
The Point Counter, Washington, January 1953

Summary of Conference Minutes

Transmitted herewith is a summary report of the conference and discussion which occurred during the internal conference of the Washington State, Telephone, Insurance, and Controller Divisions held at Olympia, January 1953, and the Point Counter, January 1953.

The discussion at these conferences was of continuing importance. The discussion was held at the first internal field meeting primarily because these were the first internal field meetings devoted entirely to the telephone program and because resulting internal audit and internal control material was presented and outlined in the field staff.

We strongly recommend that you review this material. We believe you will find it useful in promoting internal control.

Respectfully,
Assistant

[Handwritten signature and initials, possibly "L. Ferguson"]

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SUMMARY OF COMPOSITE MINUTES OF

INTERIM FIELD CONFERENCES

TELEPHONE LOANS, TELEPHONE ENGINEERING, AND CONTROLLER DIVISIONS

Held at

Cheyenne, Wyoming - December 8-12, 1952

Old Point Comfort, Va. - January 12-16, 1953

The conferences at Cheyenne, Wyoming and Old Point Comfort, Va. were held for the purpose of further presenting to the field personnel information and procedures relating to the telephone program and the resolving of general and specific problems of field personnel; also, they specifically presented to the staff of the Division of the Controller an excellent opportunity to improve its understanding of the policies and procedures relating to the various phases of the entire REA telephone program. In addition, there was presented to the field staff of the Division of the Controller specific auditing programs or guidelines to the internal auditing at the field level, and the formalized program for review of borrowers' internal control systems as an aid to audit planning. Although the emphasis was placed on the telephone program, some of the discussions in the Division of the Controller meetings were applicable to both the telephone program and the electrification program and some were applicable only to the electrification program.

It will be noted that the following remarks embody a composite summary of the presentations of the subject matter and discussions at both conferences.

GENERAL SESSIONS

The conferences were opened by general sessions, with Claude R. Wickard, Administrator, presiding.

Mr. Wickard, in his opening remarks, stated that, although we have met with rather vigorous opposition, we should, nevertheless, direct our full attention toward bringing service to rural people under the Act. "As public servants," he pointed out, "we must work to the best advantage of the people". He reported on the progress which has been made in working with the state and national telephone associations, and on the status of loan funds for the telephone program. He emphasized that our goal in the telephone program is reliable, yet economical service, and that we should pass on to the borrowers any ideas which may lead to more economical and efficient operation.

The progress of the telephone loans program was reported on by Richard A. Dell, Chief, Telephone Loans Division. Mr. Dell stated that our efforts at the present time should be concentrated on allocating available funds where they can be put to immediate use.

Hoburg B. Lee, Assistant Chief, Telephone Engineering Division, reported on the progress of telephone engineering and construction. He stated that

the groundwork has been laid for great construction progress in the immediate future since we have been successful in obtaining the general acceptance of our construction standards.

Donnan E. Basler, Electronic Engineer, reported on policy statements, borrowers' bulletins, and staff instructions. He explained the uses of the bulletins and instructions and gave a comparison of them with the present Administrative Bulletins.

The discussions on Divisional responsibilities were presented by Donnan E. Basler, Richard A. Dell and Hoburg B. Lee. The emphasis was placed on the importance of pre-loan work.

E. F. Renshaw, Assistant Chief, Telephone Loans Division, discussed area coverage surveys. He stated that the area coverage survey is one of the most important factors in writing up loans, but it has been difficult to convince borrowers that it implements the law requiring the widest possible service to rural people.

The policy of REA relative to switcher lines was discussed by Riggs Sheppard, Assistant Administrator, and Donnan E. Basler. It was stated that our present policy is to hold the number of loans which include the construction of switcher lines to a minimum.

Edward Maddox, Assistant Chief, Telephone Loans Division, Thomas J. McDonough, Connecting Company Specialist, Telephone Engineering Division, and William A. Ricketts, Head, North Central Section, Telephone Loans Division, presented the discussions on Extended Area Service. It was stated that it is felt that extended area service would probably require 80% usage by subscribers to assure feasibility.

The subject of connecting company problems was discussed by Thomas J. McDonough. He stated that agreements with connecting companies covering extended area service and relevant matters are very important, but that it is being left to the individual companies to negotiate the best agreements possible.

K. Wilde Blackburn, Associate Solicitor for Rural Electrification, and Louis A. Roland, Office of the Solicitor, discussed the problems of acquisitions and non-duplication. It was pointed out that the RE Act requires "no duplication of lines, facilities, or systems."

Donnan E. Basler and Hoburg B. Lee presented the discussion on joint use. It was stated that the broad problem is to effect the most equitable means of working out joint-use agreements between electric cooperatives and telephone cooperatives, and that joint use presents both economic and engineering problems.

The subject of manager selection was discussed by Harold F. Clark, Head, Western Section, Telephone Loans Division. The importance of field representatives' furnishing all pertinent information available was stressed.

The subject of operating agreements with electric borrowers was discussed by Donnan E. Basler. It was suggested that field people avoid making any recommendations as to joint management.

A discussion of right-of-way and easement procurement was presented by Hoburg B. Lee. He stated that procurement of rights of way and easements is the responsibility of the borrower and that it is of prime importance.

Discussions on clearing up all conditions of loans and legal problems incident to release of funds, commission jurisdiction, and commission hearings were presented by Richard A. Dell, Hoburg B. Lee, and Louis A. Roland. The major conditions to be met were pointed out, and the field personnel were urged to give any necessary assistance to the borrowers in meeting these conditions.

The collection of equity and coordination with construction was discussed by Donnan E. Basler. He pointed out that it is important for the borrower to set up a definite program for the collection of equity, and that such program should be coordinated with the completion of construction.

Leslie Surginer, Controller, and Virgil P. Russell, Telephone Accounting Specialist, Division of the Controller, presented discussions on accounting and auditing problems. The assistance of all telephone field people, regardless of division, was solicited in impressing upon the borrowers the necessity for adequate and accurate basic records. It was pointed out that the Telephone Loans Division, particularly, has a basic responsibility for promoting good records as a major factor in the adequacy of borrowers' management for which it is directly responsible.

The subject of preparation for cutover was discussed by Walter E. Rich, Head, Southeast Section, Telephone Loans Division, and James L. Robb, Outside Plant Specialist, Telephone Engineering Division. It was pointed out that one of the most important steps to be taken by the borrower in promoting good subscriber relationship is to develop a well organized and publicized celebration on the day of the cutover.

James L. Robb presented a discussion on plant records in which he pointed out the need for the installation of basic records prior to the cutover date.

Henry C. Starns, Chief, and Hans S. Hoiberg, Training Officer, Personnel Division, discussed REA personnel matters and answered questions on employee problems from the floor.

Individual section meetings, presided over by Section Heads of the Telephone Loans, Telephone Engineering, and Controller Divisions were held. At these meetings individual borrower problems were discussed.

The reports by the chairmen of the meetings held for the purpose of presenting constructive suggestions revealed there were no suggestions from the Controller's Division, but all joined in thanking Mr. Wickard for his efforts and interest in obtaining an increase in the per diem rates. Also, the Payroll, Leave and Retirement Unit was commended for its promptness in supplying REA employees with information relative to earnings and withholding taxes on Form W-2.

The closing remarks were made by Mr. Wickard at the Cheyenne, Wyoming Conference, and by Mr. Shepperd at the Old Point Comfort, Virginia, Conference.

CONTROLLER'S DIVISION SESSIONS

The opening remarks of the Division of the Controller sessions were made by Leslie Surginer, Controller, at the Old Point Comfort, Virginia, conference, and by Robert A. Stein, Assistant Controller - Examination, at the Cheyenne, Wyoming, conference.

In his opening remarks, the Controller urged his staff to take more and more interest in the broader aspects of the REA programs as a balance to the interest naturally shown in the accounting and auditing phases of the programs. He stressed the importance of examiners' field reports and urged caution and careful thinking in their preparation. He pointed out that an examiner's personality, judgment, degree of tact, etc., are equal in importance to his technical abilities, and that his relationships with people are a vital factor in the successful pursuit of his work.

Mr. Surginer stated that the telephone program must and will receive first attention from the manpower standpoint. Next in order of importance are accounting advice and assistance to electric borrowers; electric borrower operation audits; and electric borrower construction audits.

It was reported that the CPA program is developing in a satisfactory manner. Examiners were advised that it is not the policy of REA to favor any firm or firms to perform CPA audits. When pinned down to the necessity of making suggestions to a borrower, at least two or three firms should be mentioned, leaving the final selection to the borrower.

Mr. Stein also stressed the importance of the telephone program and stated that the staff of the Division of the Controller must be prepared to give it their close attention in the future.

In commenting on the Internal Control Check Lists, Mr. Stein stated that they should prove to be very valuable as a working tool in presenting more effective audit reports, with a possible savings of time.

He also called attention to the tendency of the general public to scoff at Government employees. He stated that many people have no conception of the objectives or functions of REA, and that each of us, as an employee of REA, should consider himself a representative of the United States Government and do everything in his power to convince people that Government employees do have a place in the scheme of things and do "earn their salt".

Mr. Surginer and Mr. Stein both called attention to a continuance to some degree of irregularity in reporting travel. It was pointed out there is a definite tightening up on travel. The Division of the Controller is now responsible for audit of travel vouchers and for internal audits, which makes it more important than ever that care be exercised in making claims for travel. In addition to the audit made by REA, a comprehensive audit is made by GAO. Field personnel were advised to report travel facts as they occur. The traveler may not get paid for mistakes in judgment but he will not be subject to criticism.

Field Procedures and Relationships with Other Divisions and Offices

This subject was discussed by W. Bernard Loving, Rolland W. Mars, Howard C. Paine, Albert B. O'Donnell, and James J. Murphy. It was stated that the Washington office is making every effort to attain uniformity in making assignments, processing the audits, etc., but that at the present time there is some slight difference between the procedures followed in the various section offices.

Scheduling of Audits - The scheduling of audits is contingent upon various factors. The factors to be considered in scheduling electric power and distribution general audits are the date of the last audit and the condition of the borrower. It is the responsibility of the area office to have CPA audits performed, and the responsibility of the Division of the Controller to administer the program from a technical standpoint and to provide reports on the status of the program. The new CPA borrower is usually expected to select a CPA firm within 12 months, and to submit the audit report to REA within 15 to 18 months from the date of the last general audit by REA.

Construction audits are scheduled according to need, which results in approximately one-half of the borrowers being audited each year. The most important fact to be considered in scheduling such audits is the volume of loan fund transactions unaudited. Telephone audits are scheduled on a more or less individual basis, and usually on information furnished by the Telephone Loans Division. AAA assignments generally originate in the area office, the Telephone Loans Division, or the Power Division. However, many of the requests may originate with the examiners.

It was emphasized that AAA assignments, particularly in the telephone program, are a very important part of the examiner's work program. In the telephone program, such assignments will involve a large amount of instructional work and even some bookkeeping. The amount of the bookkeeping to be done will be governed by the circumstances, but every effort should be made to keep it at a minimum.

Examination Staff of Controller's Division - In commenting on the relationship of the examination staff with other divisions and offices, it was pointed out that Mr. Surginer, Controller, is in charge of the accounting and examination functions of REA and Mr. Stein is in charge of the examination staff, who are responsible for audits of borrowers' records, and internal audits. The examination supervisors have full responsibility for the accomplishment of work in their areas. Their responsibility for audits and audit work now is greater than in prior years. They are also required to work closely with the general field representatives and representatives of the Telephone Loans Division. Examiners share the responsibility of carrying out the work of the examination section under the direction of the examination supervisor. When examiners have questions with relation to their work, such questions should be submitted to the examination supervisor.

It was stressed that audits should be completed before the examiner leaves the office of the borrower. If an extension of time is required, the examination supervisor may approve three days, the examination manager may approve five days, and any extension of time beyond five days must be approved by Mr. Stein.

In the general discussion period the following questions and answers were recorded.

1. Q. Does the field examiner's Weekly Time, Itinerary and Progress Report go to the line division office when an examiner is on a AAA assignment?

A. No. Housekeeping reports and memoranda go to the examination manager.

2. Q. Should special efforts be made to expedite the forwarding of Weekly Time, Itinerary and Progress reports, and Field Activities Reports?

A. Yes. Field Activities reports should be forwarded upon the completion of an assignment. It is doubly important to forward FI209's promptly because of information relative to itinerary. It is advisable to show itinerary as far in advance as possible--even beyond the two weeks. Mr. Surginer urged the preparation and mailing of FI209's at the close of the Friday work day.

3. Q. Does the examiner write a letter to the manager, outlining his recommendations, at the completion of an audit?

A. No, but the examiner may, when recommendations are indicated, make a summary of them and forward it with the audit report to the examination manager with a note requesting that the recommendations be transmitted to the borrower, if deemed appropriate.

4. Q. Is an Auditor's Daily Time Report (Form FI275) needed on a AAA assignment?

A. No.

5. Q. Should the examiner know what he is supposed to do before he reports for a AAA assignment?

A. Yes, if at all possible.

6. Q. Should the examiner attempt to hold to firm dates on AAA assignments?

A. He should strive to perform the work at the time assigned for it. However, assignments ordinarily should indicate a definite brief period during which the work is to be performed rather than specific dates. This will provide for a necessary measure of flexibility without weakening administrative control of the field activities.

7. Q. Should the Field Activities Report on CA assignments contain comments with respect to personnel?

A. Yes. The situation is the same as when preparing Field Activities Reports in connection with operations audits.

8. Q. Is the examiner permitted and/or required to make journal entries when on a CA assignment?
- A. This depends on the individual circumstances. Where adjusting entries of a significant nature are indicated, such entries should be made available to the borrower's personnel with a full explanation and a suggestion that they be placed in the books.
9. Q. May journal entries be made to correct a CPA's audit entries?
- A. Yes, if the condition is of serious nature and would affect balance sheet items to an appreciable extent. However, the proposed entries should be submitted to the examination manager. If deemed proper, a copy of the entries will be sent to the cooperative with the suggestion that they be entered on the books, and a copy will be sent to the CPA.
10. Q. When an examiner gives one-day accounting advice and assistance at the request of the GFR, may a copy of the Field Activities Report be furnished to the GFR by the examiner? Who prepares the assignment schedule?
- A. Yes, but when this is done, a note to that effect should be made on the bottom of the Field Activities Report. The examiner prepares the assignment schedule, has the GFR place on it a statement "Assignment requested by _____", and then sends it with a copy of the Field Activities Report to the examination supervisor.
11. Q. To whom is the Field Activities Report directed when on a AAA assignment?
- A. It is directed to the area director, or Chief of the Power Division or the Chief of the Telephone Loans Division according to whether the assignment is electric or telephone. The original and two copies are sent to the line organization, one copy to the examination manager, and one to the examination supervisor.
12. Q. What is the accounting treatment, with respect to margins, of interest on Government bonds?
- A. Under present REA policy, interest of this type is treated as non-operating revenues.
13. Q. Would it be possible to revise Form 173C to allow more space for the information relative to advances and payments to contractors, with provision made to show the reconciliation with the expenditure report and general ledger? Also may the forms be prepared with snap-out carbons?
- A. We will give consideration to this request in revising this form.
14. Q. Is a letter of instructions or suggestions to be left with the borrower at the completion of a AAA assignment?

A. You are to be governed in this matter by the wishes of the division or area office to which you are detailed.

15. Q. We were told by the Administrator at the June Conferences that all field personnel should leave a letter with the borrower, summarizing the discussions which took place and presenting any suggestions. Are we not to comply with the Administrator's instructions?

A. We are not certain that the Administrator's instructions apply to staff specialists detailed to line divisions or area offices. You should be guided by the instructions issued to you by the examination manager or examination supervisor, or by information given to you by the field representative of the division or the area office to which you are detailed. It is hoped that line organizations, in making requests for the services of field examiners, will indicate at that time whether examiners are to provide the borrower with a summary of discussions and recommendations. Such action will enable examination supervisors to state in the assignment just what the examiners are to do in this regard.

16. Q. What should we do when we receive a telephone call which merely directs us to go to such-and-such place to assist a borrower in obtaining some money?

A. Do the same as on any other assignment and give the details of the necessary work in the Field Activities Report. However, in general we are entitled to know the scope of the assignment in advance.

17. Q. When on telephone assignments, what should we do when we determine that the borrower needs assistance?

A. Where you see the need for accounting advice and assistance, the need should be recognized and action taken through the examination supervisor.

Billing and Collection Procedures in Telephone Organizations

Ralph M. Hyle of the Operations Division presented the discussion on this subject. Mr. Hyle, who is the owner of an operating telephone organization, spoke from his own experience with billing and collection procedures. He stressed the importance to an organization of making collection of the amounts due from subscribers, and pointed out that, as tools to implement the collection of and proper accounting for revenue, the basic requirements are: (1) application form, which provides application for service and office information; (2) service order, which provides information for installations, plant and traffic records, and rental charges; (3) subscribers' ledger, to record all charges and credits by telephone number and name; (4) toll statements, to itemize toll usage and tax; (5) monthly bill, to make known to the subscriber the amount owed and to provide information to the cashier; and (6) cash payment record, to record payments.

In the discussion of stub accounting versus ledger accounting, it was brought out that stub accounting is not as practicable for the use of cooperatives, which must take cognizance of the need for accumulative totals of members' usage for capital credit purposes, as individual ledger cards or ledger sheets.

It was pointed out that the FCC requirement for retaining toll tickets is six months, but, as a practical measure, they should be retained until after an audit has been performed.

In the general discussion period the following questions and answers were recorded:

1. Q. Are toll statements prepared in duplicate?

A. Generally not.

2. Q. Are collection reports to be made for each exchange, or just one for the general office?

A. If collections are made at each exchange, then each exchange should make a collection report.

3. Q. Is the collection sheet used as a posting medium?

A. No. The stubs are the posting medium.

4. Q. If the collection sheet is not used as a posting medium, what purpose does it serve?

A. It has a tendency to reduce errors, and provides a medium to furnish information on collections other than those covered by subscribers' bill stubs, as well as information as to the bank deposits.

5. Q. How are NSF checks accounted for?

A. Through the General Ledger to an accounts receivable or NSF Check account. They are not charged back on the subscribers' ledger.

6. Q. Why is the requirement by FCC for the retention of toll tickets only for six months?
- A. The reason for this ruling is not known, but the requirements were checked with FCC and the period of time is correct. The ruling may be found in Part 45 - Destruction of Records, in the FCC regulations.
7. Q. If the ruling by FCC relative to the retention of toll tickets were followed by REA borrowers, wouldn't it hinder the examiner in making the proper investigation during an audit of the borrower's records?
- A. Agreed that this is true; and that other Government agencies may require that they be retained for a longer period.

Internal Auditing

Joseph P. Flannery, Audit Policies and Methods Specialist, USDA Office of Budget and Finance, attended the Wednesday morning session of the Division of Controller at Old Point Comfort, Virginia, and addressed a few words to the group on the subject of Internal Control. He told of the interest of the Office of Budget and Finance in internal audits, and stressed the importance of having a well-planned program. He cited the case of a Government agency which, without sufficient planning, launched an internal audit program and failed in its objectives. Because of the lack of proper planning, the reports rendered failed to convince management that it was worth while. The Office of Budget and Finance is now interested in the start REA is making in the performance of internal audit in the field and is looking forward to its final culmination in a successful program.

The subject of internal auditing was discussed by Robert A. Stein, W. Bernard Loving, Howard C. Paine, Elton L. Bennett, and K. L. Culver.

General Considerations - This phase of the subject of internal auditing was presented by Robert A. Stein and W. Bernard Loving. The internal audit instruction booklet was introduced, and a short resume of the problems encountered in its preparation was given.

It was explained that several false starts were made before agreement was finally reached as to the proper method to be used in presenting the examiners with a workable program by which the objectives of the internal audit may be attained. The internal audit is one of many tools, including accounting, budgeting, organization methods, and internal control, employed by management to check up, through the layers of delegated authority, on the functioning of an organization. Internal control is woven throughout all management controls, but the internal audit is the final control which assures management that the internal controls are functioning. Congress, through the Budget and Accounting Procedures Act of 1950, has made it more or less obligatory that all agency accounting include Internal Auditing. The internal audit, within the operational functions of the REA organization, affords us the opportunity to discover our own errors, and determine the areas of required improvement, prior to GAO audit. It also provides GAO with a means, if desired, of shortening or reducing the operation of its audits through its review. The internal audit in the field reveals the degree of compliance with and the effectiveness of plans, policies and procedures, as carried out by REA, and demonstrated through the final results of the acts and procedures of borrower personnel. In other words, it is the bridge which spans the gap between the responsibility delegated to representatives of REA, through Administrative Bulletins, and the objective of REA, which is the maximum in service for the rural people served by REA borrowers. Thus, the internal audit enables the Administrator to judge the effectiveness of the agency's policies and procedures, and the degree to which such policies and procedures are carried out by agency representatives, to meet the requirements of the RE Act. Attention was called to the talks of the Administrator, and John S. Cooper, Jr., Deputy Director, USDA, Office of Budget and Finance, in the summary of the June 1952 Conferences. In his talk, Mr. Wickard stressed the point that the examiner is an "observer", not an "investigator." He is to observe basic departures from approved policies and procedures and, particularly, to observe the areas

for improvement in procedures. However, the function of the internal auditor is to disclose the areas for improvement, not to develop remedial procedures. It was pointed out that this new phase of the examiners' responsibilities provides for internal auditing in conformance with the definition of internal audit by the Institute of Internal Auditors - that is, independence, rendering protective and constructive service, and dealing to a degree with matters of an operating nature. The need for caution in dealing with matters of an operating nature was stressed. In closing, the ten points summarizing Mr. Wickard's talk at the June Conferences were discussed. The ten points are:

1. Be informed on policies, plans and procedures.
2. Don't try to be an expert in any field in which you are not technically qualified.
3. Be observers--not investigators.
4. Make specific investigations only when specifically assigned to do so.
5. Be discreet - avoid arguments.
6. Don't report the trivial - be factual and report the important.
7. Keep your own conduct above reproach and suspicion.
8. Report the commendable as well as the unsatisfactory.
9. Report on results and effectiveness rather than on personalities.
10. Don't be a "snooper"; on the other hand, don't be "blind".

Specific Auditing Programs - This phase of the subject of internal auditing was discussed by Elton L. Bennett and W. Bernard Loving. It was stated that the term "Audit Program" as used in connection with the REA field internal audit could very easily be misleading and, unless we view the term in its broadest sense, the use of it could cause us to get the wrong concept of the method of carrying out our responsibilities with respect to internal audits. We, as auditors, usually think of an audit program as an outline or description of the physical, active procedures to be undertaken in making an audit. The term also, of course, applies to the work itself, as well as to the written description. The specific programs for our internal audit function are programs only in a broad sense. They are intended to serve as guides for use in carrying out the function, but are not in any sense intended to be step-by-step procedures. There is no relationship between the programs and the chronological order in which the various phases of the internal audit are to be accomplished. It is to be kept in mind that, with very few exceptions, the programs do not set forth things to do in terms of action. It is not intended that the internal audit will involve any detailed research, special analysis, or intensive review, but that it will be made concurrently with the regular examination and ordinarily will not extend the over-all examination time to a great extent.

It was explained that, in approaching the preparation of a procedure for internal audit, no precedent could be found for the type of internal audit to

be conducted in the field by REA, and therefore the program that has been formulated is unique in that respect. Since all REA activities are covered by policy bulletins, we had the advantage of having the bulletins to study - also these bulletins will serve as a guide while making the internal audit. The procedure for internal audit has been pursued on a segment basis, or on the basis of REA activities which it is believed can be audited or appraised by the examiner. The activities of REA have been tentatively divided into nine segments, or activities, for internal audit purposes. These are listed on page 8 of the instruction booklet handed out. It was felt that these nine segments, or programs, will cover all REA activities, but we are not yet sure whether two or more might be combined, or whether activities will have to be added. Information received from the examiners will influence the changing of this list or the conclusion that it should stand as it is. The order in which the activities are listed is not necessarily significant, nor does it have anything to do with relative importance.

Of the nine internal audit activities listed, it is only the first three for which detailed audit programs or guide lines have been developed. It is not intended that the examiner will necessarily make a special effort to cover all nine of the activities in each audit. He should, however, be familiar with the activity segments, and have an understanding of the factors considered significant in REA's relationship with borrowers in connection with each of the activities. He should be alert to observe any items relating to any of the activities, and should be prepared to interpret his observations. The final report, however, may cover only two or three of the activities.

In the three activities for which guide lines for internal audit have been developed, the speakers explained that it will be noticed that the Objectives of Internal Audit are essentially the same, and that the objectives are divided into two main categories. The audit programs are also divided into the same two categories. The first - to provide a basis for appraisal of the effectiveness of REA activities - deals primarily with the status and progress of the borrower insofar as the activity is concerned. Thus we look at the final results first. We look at the final results, not from the standpoint of auditing the borrower, but because the final results reflect the effectiveness of REA activities. This portion of the internal audit program deals only with results, and is not concerned with the "why" at this point. The use of "provide a basis of appraisal" instead of "make an appraisal" in the first main category of the objective is in keeping with a point in Mr. Wickard's talk at the conferences last June. He said, "Don't try to be an expert in any field in which you are not technically qualified". We can observe, and report our observations, and show our own conclusions from such observations, but the final appraisal of the effectiveness must be made by persons technically qualified in the particular field. The second portion of the Objectives of Internal Audit and the Audit Program deals with the manner in which the specific REA responsibilities are being discharged (by REA representatives). We can profit, it was stressed, by reading this portion of the objectives over and over - through observation to ascertain, insofar as practicable the degree of adherence to the Administration's plans, policies and procedures.

Internal audit in the field may be summed up as being (1) an appraisal of the status or progress of the borrower for the purpose of determining the effectiveness of REA activities in giving advice and assistance, and (2) an appraisal of the degree to which the stated responsibilities of REA representatives

have been carried out in what we call adherence to Administrative Policies.

In discussing the features of the detailed Audit Programs, certain considerations were pointed out which revert back to Mr. Wickard's statement, "Don't try to be an expert in any field in which you are not technically qualified". Under Borrower's Records and Internal Control will be found such phrases as, "review records"; "determine whether internal control"; and "form an opinion as to". These are positive instructions to the examiner in which he is asked to determine whether advice and assistance fully met the needs of the particular situation because he is a technician in this field. Under Technical Operation and Maintenance, and Power Use, such phrases as "through observation to ascertain"; "observe any factors"; "be alert to"; and "observe what action" are used. These phrases do not instruct the examiner to make a determination as to the condition and operating efficiency of the electric plant, or whether the borrower gives sound advice to its consumers with regard to the beneficial and profitable use of electric energy. They merely instruct the examiner to observe certain conditions which will enable technicians in those fields to make the decision as to whether the advice and assistance given the borrower fully met the needs of the situation.

It was stated that a clearer concept of the Internal Audit Program as a whole is obtained after the manner of reporting is fully understood.

Reporting - This phase of Internal Auditing was discussed by K. L. Culver and Howard C. Paine. In the discussion of internal audit reporting, it was stated that the problem of putting the examiner's findings down in writing and presenting them in the clearest and most effective manner in a written report sounds relatively simple but in some instances it may be found most difficult. In any event, it is extremely important, for in the adequacy and reliability of these reports lies the value of the internal audit program to REA. There must be clear channels of communication for the full exchange of significant information between divisions or units to ensure coordination and develop satisfactory plans to improve the effectiveness of operations in the organization. The written internal audit reports provide such channels from examiners to section heads, division chiefs and all the way to the Administrator and his immediate staff.

It was pointed out that in considering the function of reporting, it is important to consider the official to whom the examiner reports. In a recent meeting of the Federal Government Accountants Association, Mr. Victor Z. Brink, Assistant Controller of the Ford Motor Company and a founder and past president of the Institute of Internal Auditors, Inc., discussed the meanings behind the definition and objectives of internal auditing. In commenting on the reporting function, Mr. Brink said that where and to whom an internal auditor reports determines his responsibility in the organization; if he reports to a bookkeeper, then his responsibilities can be no greater than those within the province of a bookkeeper; if he reports to a board of directors of a large corporation, then he is reporting to the very highest authority; but in that event, he usually would not be reporting to persons who could make the greatest use of his reports. Generally, his work would be more effective if he reported to a representative of active management, rather than to a representative of general policy-making bodies. In Mr. Brink's opinion, the internal auditor would, under ideal conditions, report to the top financial men in the

organization. Our situation definitely approaches the ideal, from that standpoint, since we do report to the Controller of the organization and our reports will be utilized by top financial and top operating management. The statement, "In the adequacy and reliability of these reports lies the value of the internal audit program to REA" points up a very fundamental philosophy. It is just plain common sense, because it is obvious that the internal audit report cannot be worth much to anyone unless its findings and conclusions are made known to the right persons in the right manner.

Our reports are not only extremely useful in bringing about the exchange of important information between organizational units but present appraisals of how things are progressing with respect to conformance to policies and plans. As is indicated in the instructions for Internal Audit Reporting, the reports are not a "one-time", or even a "sometime", thing; instead, they constitute a permanent record which can conveniently be reviewed or discussed at any time by those who are responsible for directing the REA program. We are hopeful that we will not only be able to point out deficiencies but actually provide suggestions which will enable REA to improve its procedures and their application.

Mr. Culver mentioned that J. Rhoads Foster and Bernard S. Rodey, in their 1951 Prentice-Hall book entitled Public Utility Accounting, commented as follows on internal audit reporting: "The report should marshal in logical sequence the facts to be presented. It should be concise, lucid, and interestingly written as far as may be possible. In general, such an audit report (1) states the objectives; (2) identifies the records and period covered; (3) defines the extent and nature of the examination; (4) summarizes the examination steps; (5) analyzes the figures being reviewed; (6) states the comments and conclusions as to the correctness of the figures checked and explains questionable items; and (7) states any recommendations as to needed changes in methods or procedures."

He went on to say, giving consideration to our somewhat unique circumstances, it seems we have followed those basic principles rather closely in the development of our proposed form of internal audit report.

It is extremely important for the examiner to have a clear understanding of what goes into Parts 3 and 4 of the report and the definite distinction between the two informational presentations.

In referring to Part 3 on page 28 of the instruction booklet he stated that we find the sample report presents some very general comments on the effectiveness of the records, TC & M, and power use. The comments relative to Borrowers' Records and Internal Control point out that the records are not considered complete and reliable; that sufficient personnel is employed to keep them, but the personnel is poorly trained; that little progress has been made in correcting deficiencies reported in the previous audit; and that REA has apparently directed no attention to the records and related procedures since that time. A number of recommendations are then set forth, calling for action by REA along certain lines to achieve certain objectives with respect to the records.

The foregoing, Mr. Culver continued, should be contrasted with the type of information on Borrowers' Records and Internal Control presented in Part 4 on page 30 of the instruction booklet. Here the comments become detailed and specific. It is pointed out that material records are faulty; that difficulty has been experienced in keeping consumers' transaction records accurately; that membership records are incomplete; and that expenditure reports had not been submitted for six months. Specific comments are made on statistical and other records, adequacy of staff and internal control. From this, it should be apparent that Part 3 of the report is to provide general recommendations for quick reference and general application for overall improvements, whereas Part 4 is available to provide the details to substantiate the general recommendations to be given for securing improvement on various individual phases of records and operations.

In making the presentation of information, as outlined in Parts 3 and 4 of the report, it was stated that we must not lose sight of the fact that the pattern for the various comments on borrower operations is designed to bring out the status of REA's attitude and actions with reference to the phases of the borrower's progress which constitute principal responsibilities of various operating offices and staff members. There is no doubt but what the information on borrower progress in itself is useful to REA and that it is an important adjunct to the report on REA activities, but it is actually only an adjunct to the basic purpose of the internal audit report and should always be so recognized. It is apparent that there has already been some misunderstanding on this point on the part of some representatives of other divisions who have commented on our new field function of internal auditing.

The examiners were requested to direct careful attention to the basic guidelines and related instructions set forth on pages 24 to 27 of the instructions.

In preparing the report, an original and two copies, all on white bond paper, will be required and no other copies should be prepared. The original goes to the examination manager, one copy to the examination supervisor, and one copy is retained by the examiner. They must be typewritten, double spaced, and signed.

During the floor discussion on Internal Auditing, the following questions and answers were recorded.

1. Q. Are we certain, as examiners, that we are in a position to make the statement, "It appears that REA has done everything that could reasonably be expected in assisting this borrower with a power-use program"? (page 29 of Instructions)

A. We believe the examiner is in a position to make this observation. The examiner must be the judge. We do not want you to make a statement on anything which you feel you cannot support. Confine comments to what a reasonably prudent person could ascertain.
2. Q. Where are we to find copies of reports of other division representatives? Will they be in the field files?

A. An attempt will be made to secure the cooperation of other divisions to the extent of furnishing the examination manager with copies of travelers' reports prepared by other field representatives for field files.

3. Q. Are we to proceed with all nine program activities of the Internal Audit Program from this date on?
- A. Yes. Generally, the examination supervisor will instruct the examiner as to which activities are to be emphasized, but this does not restrict the examiner from covering any other activities.
4. Q. What is the difference between the Internal Audit Report and the Field Activities Report?
- A. There will of necessity be some duplication in these two reports. The Internal Audit goes beyond the comments brought out through the Balance Sheet Audit. Some time in the future we may have to change the outline of the Field Activities Report, but until further specific instructions are given, the Field Activities Report will follow the usual pattern.
5. Q. Why are only an original and two copies of the Internal Audit Report required?
- A. Because we do not wish to distribute the reports generally, until the examination manager has had an opportunity to review them for propriety.
6. Q. Are other REA representatives leaving a copy of the summaries of matters discussed and instructions given with the borrowers?
- A. They are all required to do so.
7. Q. May we ask the manager for file copies of the reports of other REA representatives?
- A. We could not insist on it. Tactful conversation with the manager may lead to his showing you such reports.
8. Q. How are we to know that Proof of Right of Way has been sent to REA by the borrower's attorney? Would it be advantageous to contact the Office of the Solicitor for confirmation of this matter?
- A. Yes, this can be done when we feel that it is necessary.
9. Q. Is not the objective of the Internal Audit Program to see that Administrative policies and procedures are being carried out effectively and implemented?
- A. That is correct. We should advise the Administrator of any factors which indicate that policies and procedures are not being carried out, or of indications that they are not workable, so that corrective action may be considered.
10. Q. May we ask questions of technicians?

- A. Yes, generally, but not for the specific purpose of pumping information for a report. (It was stressed that we are to be in the field on an internal audit principally to help line people do a better job.)

11. Q. How will the Internal Audit Program help the borrower?

- A. The financial audit will help the borrower directly, whereas the Internal Audit will indirectly help the borrower through the improvement of REA operations. (Mr. Surginer stressed the fact that we must be cautious and avoid serious mistakes, but that doesn't mean we are not to push the program.)

12. Q. Should we report on all major functions?

- A. Not necessarily. Also, the audit programs are merely guidelines.

13. Q. How long should reports be?

- A. Just cover critical items, but use judgment when something needs expanding.

14. Q. How about borrowers' learning of our Internal Audit function?

- A. It is not necessarily to be kept secret. If it comes up in normal conversation, inform them of it but do not brag about it.

15. Q. How do we learn what the procedures of other divisions are?

- A. REA Bulletins will disclose borrower relationships. As to Staff Instructions, the Section office will receive two copies of such instructions pertaining to other divisions and we will excerpt applicable portions and inform the field people.

16. Q. Will the examiner be furnished any field folders of other divisions?

- A. This has not yet been fully resolved. It will be taken up with the Executive Officer. The present thinking is that it is not justified. The examiner should take specific matters up with his own office to get necessary information. The situation requires study to see if there is any real need.

17. Q. Will Internal Audits be made in relation to telephone borrowers?

- A. We are starting with the more familiar electric program borrowers, but we will get into telephone internal auditing as soon as possible. You should start now using the guides to the extent applicable. Nothing specific has been developed with relation to telephone borrowers and only three of the nine major program activities for electric borrowers have been developed. We would like for the examiners to proceed on their own initiative as we need the benefit of the thinking in the field to develop the procedure further. We solicit your suggestions on the remaining

major program activities, as well as on what has already been developed. This is a partnership deal--you supply the ideas and we'll codify them.

18. Q. What will REA do with the reports?
- A. The examination manager must determine what will be of value to top management. The reports considered of value will be distributed--to the line organization, to the Administrator, to the Executive Officer, to the REA Internal Examination Section, etc. Reports must be such that we can discuss them with responsible parties. We will try to establish patterns from the reports with respect to what some of the major deficiencies may be. In addition, we hope to make a quarterly report to the Administrator.
19. Q. Will we use the check list method in making evaluation?
- A. This has been considered but the idea has not been fully developed. We may decide on an informal check list which would be used by the examiner but not turned in. The programs which we have already set out are actually in the nature of a check list rather than a step-by-step procedure. These programs are not mechanical procedures--nothing substitutes for good judgment.
20. Q. Do we report our time on internal audit separately?
- A. Yes.
21. Q. How are we to apply the internal audit program to CA assignments?
- A. Internal audits will not be so extensive in connection with CA's, but we will make such audits as are practicable.
22. Q. Has any consideration been given to dispensing with the Field Activities Report after the Internal Audit program gets into full swing?
- A. This has not been considered, but it may be, after experience in Internal Audits is gained, that the Field Activities Report will become briefer and less detailed.
23. Q. May the Internal Audit Report be submitted on Field Activities Report forms instead of plain white bond paper?
- A. No. It is suggested that you conform to the instructions as to the type of paper to be used.
24. Q. Will Internal Audit assignments ever be made in conjunction with AAA assignments?
- A. No.
25. Q. How will the Internal Audit program fit into a complex installation audit for a telephone borrower?

A. It will have the same application as during any other type of audit. If it is found that REA procedures, such as proper safeguards to the loan, have not been followed, the need for an internal audit would definitely be indicated.

The Examiner's Work From the Borrower's Viewpoint

Riggs Shepperd, Assistant Administrator, discussed this subject in a session of the Division of the Controller at the Old Point Comfort, Virginia, Conference. Mr. Shepperd's discussion was primarily based on his experiences while manager of an REA-financed Cooperative. He stated that during his managership of the cooperative he had many contacts with REA auditors, and with the managers of other cooperatives whose records were audited by REA auditors. He pointed out that the average borrowers' representatives are sincerely interested in their accounting records and in having the best possible reports at the end of the year for discussion with members of the board of directors.

In the discussion of accounting records and audit reports with the board members, it is often difficult, said Mr. Shepperd, to get all important points across and retain the directors' attention and interest, as the board members are seldom trained in accounting. For this reason, the manager needs audit reports which are factual and helpful, yet simple. Mr. Shepperd stated that he realizes this is difficult under certain circumstances, but that the borrowers appreciate the auditor's efforts to prepare audit reports with brevity, conciseness, simplicity and helpfulness.

Mr. Shepperd made the following suggestions as to the examiner's approach to his assignments from the standpoint of his relationships with borrowers' personnel:

1. You must have the ability to get along with people. Everybody likes a friendly person, and, in being friendly and tactful, the auditor will find the audit proceeding without friction. Although the examiner's work primarily deals with figures, you can't escape the fact that it also is bound up in your contacts with people.
2. The cooperative personnel have regular working hours and you should adhere to regular working hours, too.
3. Plan your work so as to avoid any unnecessary interruption in the borrower's office routine.
4. When your assignment in a borrower's office is completed, leave a forwarding address so that any mail which arrives after your departure may be forwarded to you.
5. You may accept friendly favors such as an invitation to lunch, but don't accept any expensive gifts from borrowers' personnel. They may feel a little hurt at your refusal, but you should refuse tactfully. It is believed that 99% of those proffering expensive gifts would intend nothing wrong, but it is advisable to avoid the situation entirely.

6. If a situation needs investigating, investigate it, but keep the knowledge to yourself. The manager does not expect you to be devious and mysterious, but word gets around in small towns very fast so you must exercise good judgement.
7. Before taking any type of action, be positive of your facts. If you are proved wrong, no one, including the borrower, will appreciate the action you have taken.
8. Do not give the manager the impression that everything is fine and then write a critical report. Talk the situation over with the manager, point out the things which you feel necessitate criticism, and give your reasons. He will appreciate your confidence and any help you may be able to give him.
9. The manager may ask you to help him evaluate the work he and his employees are doing. When doing so, you must be careful not to make direct comparisons between this borrower and other borrowers.
10. When deserved, give the manager a pat on the back. He likes to know when he is doing a good job as well as to know of situations deserving of criticism.
11. Be helpful in explaining forms, accounting procedures, etc. Such services are very much appreciated, and are one of the best we can render to the borrower.
12. Borrowers' personnel usually appreciate having faulty record-keeping brought to their attention - but in doing so, let your criticism be factual, tactful and constructive. Keep the discussion on a high business plane, avoid personalities, and confine it entirely to facts. Nothing is resented more than criticisms based on personalities - in permitting prejudice to creep in where facts alone should stand.

In closing, Mr. Shepperd stated that the examiners' reports are actually used very often by the Administrator's office. In cases of defalcations, etc., he said that, "we always hope that your facts are checked and double-checked to the point of being incontrovertible so that we won't have to back down on our claims and then hear about it forever afterward. The Administrator's Office likes to think of the examiners as being 100 percenters - we find it difficult to think that you can be wrong."

At the completion of Mr. Shepperd's discussion, the following questions came from the floor and were answered by Mr. Shepperd or Mr. Stein.

1. Q. Can you give us more information relative to the discussion of the audit report with the manager?
- A. (By Mr. Shepperd) They would like to have suggestions, but make sure that the suggestions are tempered with a lot of thought.

(By Mr. Stein) You owe it to the manager to let him know what you plan to report and give him an opportunity to state his position. Change your comments, if such action is justified.

2. Q. What action can be taken relative to discussing the audit report with the manager, when the examiner has difficulty in making headway with the manager?

A. Tell the manager that even though you know he won't agree with your observations you would like to have the privilege of discussing them with him anyway.

3. Q. What can the examiner do about non-itemization or non-authority on large expense items?

A. While it is necessary to check on authority, you should be careful about always demanding full itemization, because the borrower is not on the Government payroll. A reasonable breakdown, consistent with normal business practices is all that can be asked.

4. Q. Would it not be a good policy for managers to avoid signing or countersigning any checks reimbursing themselves?

A. This is a good suggestion but it would be difficult to follow 100%.

Improving Auditing Techniques and Working Papers

The discussion on this subject at the conference held in Cheyenne, Wyoming, were presented by Merrill Riggen and Rolland W. Mars.

Suggestions Resulting From Field Observations -- This phase of the subject was presented by Merrill Riggen. He stated that the improvement of auditing techniques and working papers is something the staff of the Division of the Controller has been striving for since REA first began, and that we have come a long way in establishing uniformity in and completeness of audit working papers and reports. He pointed out that in the early days of REA, before the Handbook for Field Auditors was compiled and furnished to the examiners, each examiner applied his own techniques to a great extent and, as a consequence, our audits often lacked uniformity and completeness. However, even with the guidelines laid down in the Handbook for Field Auditors and the constant striving toward perfection, we feel the need for further improvement.

Mr. Riggen commented further, as summarized below:

The handbook, if properly used, will assist us in attaining uniformity. In the performance of an audit, we are continually asking ourselves, "What is expected or required for this or that schedule or analysis to further improve our work?" There are three major features which should always be kept in mind in the preparation of our schedules and analyses. They are (1) structure; (2) completeness; and (3) extent of examination.

In making the determination as to the type of schedule or analysis to be prepared, the examiner should decide first what he expects to accomplish through the preparation of the working paper; and, second, the organization of the information on the working paper in order to achieve the desired result. It is useless and time consuming to prepare a long, detailed analysis of an account, in effect only a transcript of a ledger account, which proves nothing to the examiner and serves no purpose in the review of the audit other than to show that the balance in the account agrees with that on the trial balance. Working papers have a definite purpose and each working paper prepared should serve that purpose. Working papers should be complete as to detail; that is, an analysis of an account should show the ledger balance at the beginning date of the audit period (prior audit balance); the detailed analysis, if necessary, or the totals of the result of the analysis, if appropriate; all adjustments identified; and the adjusted balance as of the audit date. The working papers should also contain a brief statement of work done over the signature of the examiner. No working paper can be considered complete unless it provides information as to the work performed. The statement on any schedule or analysis should always be honestly stated. It will not only furnish the basic facts for writing the audit report, but will permit the reviewer in the office to gain a fuller knowledge and understanding of the accounting situation portrayed in the schedule and facilitate the review of the audit report.

Other factors pointed out by Mr. Rigger as being essential to a well prepared audit are the working paper reference column on the working trial balance, and the audit journal entries. The working paper reference on the trial balance should always be completed with either a schedule number or a journal entry reference. Journal entries should be prepared with sufficient information to support the entry. The journal entry explanation should, if an adjusting entry, refer to the original entry, giving such details as source or original entry, date, check number, names, descriptions, amounts, and accounts affected by the original entries, or it should refer to the working paper detailing the original entry involved. The explanation should present adequate justification for making the adjustments. When the explanation refers to an exhibit, schedule, or analysis, such audit working paper should be identified, and the explanation should include a statement to the effect that the borrower has been furnished with a copy. Journal entries affecting prior accounting periods should state the number of the account affected, and the year to which the adjustment is applicable. The entry should be so prepared that anyone reading the explanation can fully understand it.

Suggestions Resulting From Office Review of Audits - This phase of the subject was presented by Rolland W. Mars. In his introduction, Mr. Mars pointed out that there would obviously be some overlapping in the suggestions for improvement in auditing techniques and working papers from the viewpoint of the examination supervisor and those resulting from office review of audits, but since the review in the field of necessity is cursory, the office review should provide more in the way of the technical aspects of the desired improvements. Mr. Mars quoted from a talk given by Mr. T. A. Hoffman, CPA, and the head of the GAO audit staff group presently engaged in an audit of REA, as follows:

"Working papers may be considered as the raw material from which auditors' reports are prepared. The papers represent the connecting link between books, records, policies, procedures, and internal controls underlying the financial statements examined and the audit report submitted to the borrower. Working papers constitute the only proof of audit work performed, as well as the record of audit findings and conclusions. An auditor should look upon each work sheet as a separate report to his superior on the audit task assigned to him. Working papers can stand the test only if a superior can take the papers prepared by an auditor and prepare an audit report from the working papers without asking questions. If your working papers can stand this test you will have done a proper job.

"Whether the report is prepared by a superior or by the auditor himself, there should be no difference in the preparation of working papers, conduct of the audit, or appraisal of internal controls. An auditor does not perform these functions solely for the purpose of reporting to himself. Others must rely on his work."

Mr. Mars stated that the requirements for adequate and proper working papers, as set forth in the quotation from Mr. Hoffman's talk, represent a challenge to any examiner - and only the best successfully meet the challenge. Too frequently examiners accumulate too many working papers containing useless information, or present papers too brief to offer conclusive evidence that they have made a complete and satisfactory audit. In addition to the general requirements for adequate and proper working papers, he pointed out that the working papers prepared by REA examiners serve other purposes, such as (1) a source of information in subsequently discussing findings with boards of directors; (2) assistance to the examiner in defending his position from criticism; (3) basis for review in Washington office of the work of the examiner to see that statements and schedules have been properly prepared and supported, proper standards have been followed, procedural technique has been proper and adequate, and that comments and recommendations in the audit report are adequate, proper, and reasonable; (4) a guide to succeeding examiners; (5) a reference for use in working out specific problems on certain borrowers, it sometimes being necessary to refer to audits performed as long as ten years previously; and (6) an aid when one examiner must leave a partially completed assignment and turn over the completion of the audit to another examiner. (Mr. Mars stated that, in this instance, if the second examiner can pick up the work and proceed without confusion, the working papers have successfully met the test.)

Mr. Mars presented the following questions as being ones which the examiner may ask himself as a guide in the preparation of audit working papers:

- (1) Are these data necessary to the report?
- (2) Are they necessary to the support of any item in the report?
- (3) Are they necessary in the event of a future investigation?
- (4) Are they necessary for verification of the correctness of records and transactions?
- (5) Will their omission have serious consequences?

He gave the following suggestions for improving auditing techniques and working papers resulting from the review of audits in Washington:

- (1) Every working paper should reflect work performed and verifications accomplished.
- (2) Avoid mere transcripts of general ledger - give references and sources.
- (3) Give full description of work performed on scope of verification of cash transactions. Do not use check marks or merely say "sufficient".
- (4) Make certain all balances on working papers agree with final balances on working trial balance and audit report.

- (5) Make certain margin balances by years are supported by working papers and agree with comparative schedule in report, as well as Schedule 2.
- (6) Breakdown of accounts receivable-either in working paper schedule should support amounts shown in report. Great difficulty is experienced in some cases in making reconciliation.
- (7) Analyses of construction accounts should contain reconciliation of charges for payments to contractor and engineer with expenditure report.
- (8) Explanations on audit adjusting entries must be explicit and contain complete reference sources as to amounts and items involved.
- (9) Index should be carefully prepared to provide ready reference during review and subsequently. Some cross - indexing may be desirable.
- (10) Physical inventories of material and supplies should be reconciled to "as of" date of audit, when the count is made at other than "as of" date.
- (11) Suggests that on the first audit of a telephone borrower, working papers include list of various books and records and other important data available for examination.
- (12) Where a telephone borrower's records are scanty, or general records of account do not exist the audit may necessarily require a more detailed review of such records as do exist.
- (13) In some telephone audit assignments, reports to regulatory bodies may of necessity be used partially as the basis for the installation of the accounting system. If so, working papers should reflect full details.
- (14) The working papers on telephone audit assignments should contain full, detailed information concerning equity funds.

At the conclusion of the discussions, the following question and answer were recorded.

- Q. With reference to giving complete information concerning equity funds, would not the information on the expenditure report be sufficient?
- A. The statement concerning giving complete information relative to equity funds referred primarily to equity funds as related to sections. However, full information should be given concerning equity funds, especially when there is any deviation from the stated requirements.

The general subject of Improving Auditing Techniques and Working Papers was assigned to Howard S. Myster and William M. Imwalle for discussion at the conference held at Old Point Comfort, Virginia. Mr. Myster, whose specific subject was Suggestions on Techniques, was first on the program and had completed a few minutes of his discussion when he was suddenly stricken with a heart attack and passed away within a few minutes.

Because of the unexpected delays in the conference program, it was not possible for Mr. Imwalle's talk to be given.

Review and Appraisal of Internal Control

The initial discussions on the new check lists for the evaluation of internal control and its application in REA auditing were presented by W. Bernard Loving and Elton L. Bennett.

It was stated that the check list is a tool to assist the examiner in the proper study and evaluation of the internal control practices of REA borrowers, and to determine the extent of examination and audit of transactions necessary in accordance with generally accepted auditing standards. It was pointed out that one of the standards of field work that have been presented by the American Institute of Accountants as being a "generally accepted auditing standard" is: "There is to be a proper study and evaluation of the existing internal control as a basis for reliance thereon and for the determination of the resultant extent of the tests to which auditing procedures are to be restricted." Therefore, in order that our field work may meet generally accepted standards, the examiners must have made a proper study and evaluation of the existing internal control and they must have used the evaluation as a basis for reliance thereon in determining the extent of the auditing procedures.

It was further stated that there can be little doubt that proper evaluation of internal control, and gearing the audit tests to the evaluation, is one of the functions of an accountant which require the highest degree of judgement and technical knowledge. It wouldn't require a great deal of training, nor much judgment, for a person to audit a set of records by simply retracing all of the steps taken in originally building up the records. But it would take a lot of time - probably more than the original recording. It is the examiner's ability to weigh each of the factors which come within the scope of internal control - such as personalities, organization plan, division of responsibilities, and such special control procedures as budgetary and other controls - and make, through his judgement and technical knowledge of the value of each factor, a determination of the extent of time to be spent and detailed work to be done which raises his status to that of a professional as compared to the accountant who merely retraces the step-by-step accounting.

It was pointed out that there is no set rule for internal control. Internal control, even in two enterprises which appear to be identical, would never be identical - there is always some difference, some controlling factors which would result in differences. For this reason, you could not take a check list, fill it out, add up the check marks in each column and mathematically convert the results to a percentage or to the number of items to be test-checked. Nor could you use a chart to indicate that a certain number of check marks in a certain column would eliminate certain procedures or require certain additional procedures. The system of internal control must be evaluated by the application of judgment and technical knowledge.

It was further pointed out that internal control is always a matter of degree -- that is, there is no perfection in a system of internal control. Many systems of control are entirely satisfactory and some may be at the point of greatest efficiency. But for purposes of determining the extent of audit tests, we must evaluate each segment of the system, as well as the system as a whole, in relation to the phase of the audit being performed.

In closing the discussion on Internal Control, the speakers cautioned that, while it is common practice in the accounting and auditing profession to use a check list, we must be extremely careful in our approach to its use, as our borrowers are not familiar with this method, and it is also a new procedure to us. We must use good judgment and common sense in obtaining answers to the questions on the check list, so that the borrower does not become suspicious and form the opinion we are investigators. (A by-product of the check list is its use in writing comments, to re-evaluate certain operations, and as a tool for the line office - to present a picture of conditions in the borrower's office and what is needed as a remedial measure. However, it must be remembered that these are only by-products and not the primary purposes of the check list.)

Use of Check Lists by Examiners: Utilization of Data From Check Lists; and Results of Field Tests to Date -- These specific subjects of the general subject of Review and Appraisal of Internal Control were discussed by Richard Platte, Keith McKinley, Carl W. Bark, and Joseph D. Haley.

In commenting on the internal control check list and its use, the examiners reported that the check list and accompanying instructions were carefully studied and a determination made as to the methods to be used in obtaining the required information to apply to the check list. The various office procedures of the borrower were studied and discussed with the office personnel. After becoming familiar with the office methods and procedures, office policies, and the minutes of the board meetings, the examiners completed the check list as far as possible. The items on the check list which could not be completed at that time were completed later as the specific phase of the audit was entered into. It was felt that as much information for completing the check list as possible should be obtained without direct questioning of the office personnel. The importance of weighing carefully each item on the list to determine the significance of the questions in relation to the internal control and its subsequent evaluation was stressed.

The discussion of the use of the check list in the performance of audits brought out the point that without the proper utilization of the information so obtained, the examiner's time and efforts in compiling the information are wasted. Since the examiner is responsible for his opinion concerning the financial statements, he must make sure of sufficient checks to avoid criticism for lack of coverage. Therefore, the final step in utilizing the check list as a means of evaluating internal controls is important, not only from the standpoint of the time and money which can be saved through the elimination of unnecessary audit steps, but as a protection to the examiner in the responsibilities he assumes in making the audit certification.

The practicality of the check list was stressed by some of the speakers in commenting on their usage of a similar type of check list in the actual audit of the Dairyland Power Cooperative, REA's largest borrower. In the performance of this audit, the examiners went through the entire check lists to get a general picture of the audit needs. Then, in each phase of the audit, the examiners used the check lists in a more detailed manner. The lists were used not only to determine the controls in each department but they were also used to determine the controls between departments. The examiners reported that they found the check lists saved a tremendous amount of time in the performance of the audit.

During the discussions from the floor the following suggestions were made:

- (1) That Section 16 - General of the check list show the number of employees in the borrower's office. A second suggestion was made that this information be at the front of the list.
 - A. It was agreed that this information should be included in the check list but, since the information is mainly for management, it should come under the General section.
- (2) That the Internal Control check lists be divided into two parts - one bearing on REA internal control and one on borrowers' internal control.
 - A. The Internal Control check list applies only to the borrower's internal control.

As a result of the last suggestion and other remarks made from the floor, Mr. Surginer stated that there seemed to be some misconception relative to the check list. There appeared to be an inclination to give more concern to filling out the form than to making use of the information in determining the audit scope. He pointed out that the check list is intended to serve as a tool in the audit work and not as an additional report to be made. Mr. Surginer cited passages from the Handbook which pointed out that the examiner's judgment in evaluating the borrower's internal control system is the vital element. He also stated that the examiner needs to consider every point on the check lists to make a good audit, and that to fill out the check list at the end of the audit, as had been considered by some of the conferees in the discussion from the floor, is a waste of time.

The field staff was advised that the new procedure becomes effective immediately; also that it should be used in connection with construction audits to the extent applicable.

Improving Audit Reports and Field Activities Reports

This subject was discussed by Howard C. Paine and J. H. Rubenstein.

In the discussion of this subject, it was pointed out that the function of the audit comments is to interpret the facts, to add significant details, to define and explain obscure items, and to make recommendations. To accomplish this, the examiner must concentrate on essentials and refrain from cluttering up the report with trivialities. His guiding principle must be the interests and needs of the reader of the report. The audit report must also be factual and concise.

It was further pointed out that there are several faults commonly found in audit reports, one of the most common being stereotyped comments. Often the comments in the reports, or portions of them, appear to be copies from the sample report in the Auditors' Handbook with no regard for variations in the circumstances governing the subject being commented on. Other common faults in the preparation of audit reports are inconsistencies between the comments and the facts indicated by the working papers; inaccuracies in figures in the balance sheet comments; bad composition and grammar; lack of effective organization of material; use of unnecessary words; use of too many big words; and use of words of ambiguous meaning.

The examiners were advised to review the reports after they are completed to make certain the reports do not contain any of the faults pointed out. For further improvement in the audit reports, it was suggested that the examiners use simple words and short sentences, refrain from using account numbers in the audit report, and to use the general comments section of the report, instead of the balance sheet comments section, to give opinions.

In discussing the Field Activities Report, it was pointed out that the tone of some reports is often too cynical and critical. The report should be factual. It should contain information which is representative of the important facts disclosed during the audit. It should be written in such manner as to make it interesting enough to the reader that he will read to the end of the report. This is especially true when the report is of necessity a long one, as important facts may be overlooked because the report has become tiresome before the reader reaches the conclusion of the report. The use of a colloquial expression may lend color and add punch to your remarks on occasion, but such expressions must be employed very rarely and only when they would be entirely appropriate. Too many such expressions will detract from the report, no matter how well prepared it may otherwise be. Remember that a copy of the Field Activities Report is sent to the Administrator's office, as well as being used very often by representatives of other line organizations, and your work is judged to a large extent by the manner in which your report is prepared; that is, your manner of presentation, your choice of words, the importance of the material and situations to which the report pertains, and the effectiveness of the report in relation to its future use.

Auditing Procedures in the Telephone Program

This subject was discussed by Virgil P. Russell in the conference held at Cheyenne, Wyoming.

Mr. Russell gave a resume of some of the major points to be considered by the examiner when making the preliminary examination of an existing commercial telephone company. He stated that the history of the company should be given in the opening paragraph of the audit report. The information to be given would include (1) the organization date of the company, and the state under the laws of which it is organized; (2) duration of charter; (3) authorized capital; (4) type and par value of capital stock; (5) statement as to whether additional capital has been authorized; if so, type and par value of capital stock; (6) territory served, and whether rural, urban, or both; and (7) number of exchanges. This information, or as much as is applicable to the borrower, should be given on newly incorporated companies and cooperatives..

Mr. Russell mentioned the tendency of some of the smaller telephone companies to keep part of the funds collected from the subscribers in the office to make change and pay incidental expenses, and even to meet their payroll. He stated that this practice should be discouraged and recommendations made that all collections be deposited intact; that a petty cash and change fund be established; and that checks be issued to employees for salaries and wages.

Mr. Russell called attention to the variance in the practices of some of the smaller companies relative to accounting for excise taxes. He stated that in accordance with a ruling of the Bureau of Internal Revenue, it is permissible for telephone companies to pay excise taxes on the basis of collections from the subscribers, and where the company maintains adequate control over this method of reporting and paying taxes we do not suggest making a change. However, where the company does not maintain adequate control, we recommend that the method of reporting and paying excise taxes on billings be adopted. When this method is followed, it is necessary to make adjustments in the amount due the Collector of Internal Revenue when subscribers' accounts are charged off as uncollectible.

Mr. Russell pointed out that one of the requirements of obtaining an REA telephone loan is that a telephone organization be incorporated. He stated that during the recent Training Course in Washington a question came up relative to converting accounts from a partnership or proprietorship to a corporation, as to whether entries may be made to surplus and other accounts (on the partnership or proprietorship books) which would affect the income tax base. In this respect the entries are subject to the decision of the borrower. The Bureau of Internal Revenue in Washington has been contacted for a ruling and it informed us that (1) in the case of a partnership converting to a corporation, Form 1065 Partnership Income Tax Return must be filed for the period of operation under Partnership, and (2) in the case of a proprietorship converting to a corporation, Form 1040 Individual Income Tax Return filed by the proprietor at the regular time must include operating data for the period of operations under Proprietorship. Both forms, as applicable, can be filed with the Corporation Income Tax Return for the calendar year's operation. Entries of a minor nature, which affect the income tax base, should be explained by the borrower to the Bureau of Internal Revenue in a letter when transmitting the

Income Tax Return. When entries of a major nature are to be made, the borrower should contact the local office of the Director of the Bureau of Internal Revenue for advice.

Accounts Conversion From Individual Proprietorship or Partnership to Corporation

Donald B. Hase discussed this subject in the conference held at Cheyenne, Wyoming.

Mr. Hase gave a general outline of the necessary steps to be taken in making a conversion from a proprietorship or a partnership to a corporation. He pointed out that a trial balance is taken off the general ledger of the proprietorship or partnership as of the date the corporation commences operations. From this trial balance is obtained the assets and liabilities to be set up in the records of the new corporation. Also from the trial balance of the proprietorship or partnership is obtained the partners' or proprietors' equity in the business, which is to be, or has been, the basis for issuing the capital stock of the corporation.

Installation of Telephone Records for Cooperatives

This subject was presented by Marshall R. Smith, Jr., and Adrayn L. Keel.

It was stated that experience has shown that the examiners will be confronted with some situations in the installation of accounting records for cooperatives in the telephone program very similar to the situations encountered in the electric program. For example, it isn't unusual to find that in the early stages of organizing a new cooperative, the organizing committee has failed to establish a procedure which will enable the examiner, when making the installation of records, to properly identify all monies collected. But, generally, it has been found that the early records for telephone cooperatives are in better order than the early records for electric cooperatives. This is attributed to more effective guidance from REA personnel contacting the borrowers in the early organization stages, and to the assistance given to the organizers by REA electric borrowers' personnel.

It was pointed out that in commencing the installation assignment, there are certain files and legal instruments which are helpful in obtaining information required by the examiner. Following is a resume of such files and legal instruments with the information to be obtained:

- (1) Review the field file, which usually contains copies of the pre-loan recommendations and the loan contract. The pre-loan recommendations are a valuable source for providing information on the proposed system, location of exchanges, description of properties to be acquired, economic factors of the area and other data, and information relative to the estimated average annual receipts. A review of the "prerequisites to advance of funds" section of the loan contract will indicate the items for which to watch as the installation progresses.
- (2) Review the by-laws - not for the purpose of picking out legal flaws but to determine the cooperative's position as to memberships, equity, capital credits, and to discover any items which may complicate the project set-up or which conflict with REA policy.

- (3) Review the minutes of incorporators' and boards of directors' meetings. Watch for designation of board members, election of officers, designation of depositories, and the usual items concerned with employees, wages, authorities and the like.

After the review of the files and legal documents, the speakers continued, the actual writing up of the books is the next step. For the sake of uniformity in the accounting among borrowers, it is suggested that forms like or similar to those recommended by REA be used. Cooperative personnel should be utilized as extensively in writing up the books as their abilities will permit, as it enables the bookkeeper to become more familiar with chart of accounts and classification of items. The development of adequate and necessary subsidiary records and a suitable filing system is also a part of the installation assignment. The installation of subsidiary records includes membership and equity records, an adequate timekeeping system, records for the accountability for office furniture and equipment with its related depreciation reserve, perpetual inventory records for material transactions, and a billing procedure, if the cooperative has acquired, or is to acquire, an operating company and continues its operations. A step-by-step explanation of the handling of equity funds, REA advances, disbursements from the construction fund, and preparation of requisitions and expenditure reports should be given the bookkeeper and the manager.

It was pointed out that in addition to the duties entailed in making an installation audit, there is another consideration of the highest importance and that is the cultivation of the goodwill of the cooperative's personnel. By exemplary conduct, a business-like approach to our job, and by providing helpful advice and instruction in our field, we can engender respect and goodwill by the cooperative's personnel for the examiner and the REA program generally.

Installation Audits for Existing Commercial Telephone Companies

This subject was discussed by Peter Schwan, Examination Supervisor, North Central Section.

As a preliminary to his discussion of installation audits for existing commercial companies, Mr. Schwan pointed out that the primary purpose of the audit is to determine whether there has been any substantial change in the borrower's financial condition subsequent to the date of the financial statement furnished by the borrower with the application for a loan, as any substantial adverse condition may jeopardize the security of the loan. Further, it should determine whether the financial statement submitted with the loan application properly reflected the financial condition of the borrower as of the specified date. Another purpose of the audit is to determine the borrower's compliance with the loan contract requirements, particularly as to the prerequisites for advance of funds, such as the collection of equity funds, etc.

Mr. Schwan stated that there are four factors which are to be considered in the completion of an assignment for an installation audit for an existing telephone company. These factors are installation, operations, organizational structure, and contractual obligations, and they apply to all initial audits.

The examiner, Mr. Schwan stated, should familiarize himself with the loan contract, and other available information, before his arrival at the office of the borrower. Upon arrival, he should contact the person who has been notified of his visit and briefly explain the purpose of his visit. In explaining this purpose, the examiner should use the approach that he is there to render assistance to the borrower in matters of accounting, which includes installation of the appropriate system of accounts, explanation of the functions and purposes of the financial requirement statement and expenditure report, and the system of budgetary control. Mr. Schwan said that, in his opinion, this first contact is very important as it may be the deciding factor as to whether the examiner's visit is a welcome one or not. At that time valuable information may be obtained about the borrower, such as the past history of the company, territory served, and what steps have been taken toward meeting the loan contract requirements. When planning the audit work, a study of the accounts shown on the trial balance and the office routine and procedures will assist materially in determining the extent of the detailed check of transactions which will be required.

Mr. Schwan stressed the point that the examiner should be courteous and tactful, and should demonstrate a professional public accounting approach. He should avoid unnecessary conversation and the premature discussion of matters pertaining to the audit. He should avoid going into unnecessary detail by recognizing and applying the procedures and methods of control employed by the organization. Also, he should avoid direct criticism of the office procedures and accounting methods. If, after becoming thoroughly familiar with the office procedures, the examiner feels a change to bring about improvements is indicated, he should discuss the suggested change in such manner as not to antagonize the office personnel and other responsible persons. Remember that REA is only a lending agency.

During the discussion from the floor, the following questions and answers were recorded:

1. Q. Do memberships have to be identified?
A. Yes. Membership records are to be maintained with all necessary information.
2. Q. When membership fees are part of the equity funds and an amount in excess of the equity requirements has been collected, in which bank account are the excess funds deposited?
A. The membership fees required to be a part of equity for the loan are deposited in the Construction Fund account, and any collections in excess of the equity required will be deposited in the General Fund account.
3. Q. In which bank account are equity funds collected on an unapproved section of construction deposited? This question relates to an instance wherein one section has been approved and is under construction and the equity funds on the second section are in the process of being collected but for which the company or cooperative does not have to account on the expenditure report until a later date.
A. A separate bank account should be opened for these funds and they should be held intact until a Certificate of Deposit is requested by REA.
4. Q. What is the normal quantity of telephone instruments to be kept on hand?
A. There is no definite percentage recognized as a normal stock.
5. Q. What is the policy relative to capitalization of instruments when received?
A. The policy is to charge the instruments to Materials and Supplies when purchased and account for them as used. However, many small companies maintain a very small supply of instruments and capitalize them when purchased. This is contrary to good accounting, but it may be accepted as a matter of expediency where a company is too small to make it economically feasible to maintain elaborate material records.
6. Q. What is the REA-recommended rate for depreciation purposes?
A. The minimum composite rate recommended by REA is 3.5%.
7. Q. Has any information been issued on the maintenance of continuing property records?
A. Yes. This information was issued in a manual titled "Continuing Property Records For Small Telephone Companies."
8. Q. Is it the responsibility of the examiner to contact the State commission relative to accounting matters?

- A. No. The borrower must contact the State Commission on any matter relative to the borrower's business.
9. Q. What is the examiner's responsibility when a representative of the State commission contacts him relative to specific accounting questions?
- A. The examiner should answer the questions but he should confine his remarks or discussion relative to the borrower's business, strictly to the accounting questions.
10. Q. What is the policy relative to any adjusting entries to be made of a partnership or sole proprietorship when converting to a corporation?
- A. All such entries are subject to concurrence by the partners or proprietor.
11. Q. Is it proper to record the equity of partners or a proprietor in the Capital Stock account when converting records from a partnership or proprietorship to a corporation?
- A. No. A deferred credit account, Capital Stock Subscribed, should be used. The deferred credit account is preferable.
12. Q. The FCC Manual of Accounts does not provide an account for total authorized capital stock. Which account may be used to record the authorized capital stock, if such an entry is desired?
- A. Recording of authorized capital stock (except by memorandum entry) is not ordinarily recommended.
13. Q. Which is the proper account to use to record the write-off of right of way?
- A. Right of way is considered a depreciable account, but it is not mandatory that it be depreciated. It may be amortized over a period of years at the discretion of the borrower. If depreciated, the Reserve for Depreciation account will be used to record the credit; if amortized, the Amortization Reserve for Intangibles will be used to record the credit. Right of way is included in the component rates for depreciation in the REA-recommended minimum composite rate of 3.5%.

MEETING OF ELECTRIFICATION PROGRAM REPRESENTATIVES
OF THE CONTROLLER'S DIVISION

Construction Auditing and CPA Follow-up

This subject was discussed by Elton L. Bennett. He stated that in the performance of construction audit, there are three major objectives, which are:

- (1) To determine that construction funds have been spent only for approved purposes, and that the proper accounting has been made to REA.
- (2) To review the general over-all aspects of the CPA audit to determine if the audit meets the needs of REA and the borrower.
- (3) To observe generally the progress of the borrower from the viewpoint of REA as lender, specifically as to whether the general system of internal control and methods of operation are such as to satisfy you that the security of the loan is not being jeopardized.

With respect to objective No. 2, review the journal entries for propriety and conformance to REA procedures. The type of journal entries made are usually a good indication as to whether the CPA audit meets the needs of REA. If there are no journal entries, the examiner should scan the records in order to determine whether the auditor may have overlooked necessary adjustments to conform to REA procedures.

Mr. Bennett further stated that, if possible, the audit should be made as of the date of the CPA audit. If the construction audit is as of a different date from that of the CPA audit, the construction fund cash should be reconciled and a confirmation of the bank balance obtained from the depository. In performing the audit, he continued, you should satisfy yourself as to the accuracy of the general procedure relative to work orders and construction costs. It is not necessary to check every item in the construction costs as it is assumed that the CPA has verified the accuracy of these costs.

Mr. Bennett pointed out that whether the construction audit follows a CPA audit or not, examiners are to follow the procedure in the Handbook with respect to Construction Audit Following General Audit By CPA, except that in each case the construction fund cash is reconciled and bank confirmation obtained, unless the Construction Audit is as of the same date as the CPA audit.

The following questions and answers from the floor were recorded:

1. Q. It is rumored that one of the State associations will employ engineering staffs but that they have been discouraged from having a CPA staff. Why?
A. Professional standards require that the CPA give an independent opinion which could not be expected from an Association staff, as the Association is the cooperatives' own organization.

2. Q. Why could not the State associations, as well as REA, have lists of approved CPA's?
- A. REA does not approve CPA's on a general basis but only on a case basis, so there will not be such a list.
3. Q. Should cases be reported where the CPA's are making their contacts with the managers instead of the board of directors?
- A. Such instances should be reported. Our policy is to have the board of directors make the selection of the CPA, although the manager probably would make the contact with the board for the CPA. Do everything possible to discourage the manager in making the selection, and educate the board to do so.
4. Q. How far should the examiner go, in making the reconciliation of construction cash, if the Construction Audit date is different from that of the CPA audit?
- A. Make complete reconciliation and obtain confirmation from the depository.
5. Q. We are making construction audits where CPA audit has not been made. How far are we to go in reconciling cash? Should General Fund cash be reconciled?
- A. Follow the same procedure as when the Construction Audit follows the CPA audit, unless there is reason to suspect that something is wrong. In such a case, reconcile the general fund cash also. The Construction Audit covers construction funds primarily and it should be kept at that level unless there are indications that something is wrong.
6. Q. If the CPA audit were made in June and the Construction Audit were made in December, would the examiner be held responsible for not discovering an embezzlement of general funds which occurred within the interim period?
- A. No, because you did not audit the general funds.
7. Q. In connection with the audit of work order inventories, how much examination should be made?
- A. Only a sufficient test check to determine general accounting practices for giving particular attention to CPA's requirements. In general, we assumed that the CPA has checked these costs and we accept that.
8. Q. If overhead on work orders seems too high, should we check into that?
- A. Yes. Make check of one or two months to satisfy yourself if such cost appeared to be definitely out of line. In general we would expect the CPA to give attention to this matter.

Adjusting Expenditure Reports

Samuel A. Gellis, Examination Analyst in the North Central Section, discussed expenditure reports and adjustments thereto. Attention was directed to proper accounting for automatic circuit reclosers. It was pointed out that after the present budget for AC reclosers has been exhausted, future advances will be under Item 1 - Construction or Item 14 - Material, depending on whether the reclosers are purchased and installed in connection with project construction or work order construction.

Mr. Gellis stated that it is the examiner's duty to assist borrowers in preparing an adjusting financial requirement statement, when necessary, to reconcile budget purposes between the financial requirement statement and the expenditure report; also, to assist the borrower to clear small budget purpose balances which are no longer needed, and to advise the borrower of the necessary action needed to eliminate overdrafts in budget purposes.

Pertinent Points in Auditing Cash

Henry J. Froehner, Examination Analyst, Eastern Section, discussed this subject. He pointed out that while our examiners do not audit the records of borrowers primarily to determine whether fraud has been perpetrated or an employee has embezzled money, they must ever be on the alert to detect such wrongful acts. Since cash is peculiarly subject to misappropriation, it is necessary that the procedure involved in its regular handling be such as to safeguard this asset to the utmost. It is important, then, Mr. Froehner stated, that the examiner review the office procedure and determine whether a satisfactory and adequate cash control has been instituted. If the examiner determines that an adequate internal control system has been installed, he must satisfy himself that it is actually functioning. This determination is accomplished by the application of the test-check procedure. Our Handbook for Field Auditors covers this subject very thoroughly, and it is suggested that the examiners review the text thereof time and again so that they become completely familiar with it and may plan their audits accordingly.

Mr. Froehner also pointed out that in the REA examiner's audit of cash transactions, an important phase is the audit of construction fund transactions. The examiner's responsibility with respect to this phase of the audit is two-fold, as the propriety of the disbursements and their supporting evidence must be determined, as well as whether the accounting disposition and the budget classification are proper.

CLOSING OF THE CONTROLLER'S DIVISION SESSIONS

A final discussion of Internal Audit and Internal Control was led by Robert A. Stein. This discussion was helpful in bringing about a better understanding of these two important subjects.